

Kentucky Agriculture Finance Corporation

Meeting Minutes

February 19, 2003

The Kentucky Agriculture Finance Corporation held their first meeting at 9:30am on February 19, 2003 in the Paul P. Borden Conference Room in the Kentucky Higher Education Assistance Authority Building in Frankfort, Kentucky.

Members Present:

Mr. Gordon Duke; Mr. Doug Lawson; Ms. Jane Jones; Mr. Billy Hurd; Ms. Sandy Ross; Dr. Harold Benson; Ms. Annette Crawford Walters; Mr. Wayne Hunt; Mr. Charles Miller; Mr. Bob D. Proffitt; Mr. Billy Joe Miles; Commissioner Billy Ray Smith

Governor's Office of Agricultural Policy Staff Present:

David Bratcher; Gene Royalty; Bruce Harper; Brad Wellons; Bill McCloskey

Guests:

Louie Rivers, Kentucky State University
George Burgess Office of Financial Management

David Bratcher announced that the press was notified of this meeting.

The board members introduced themselves in lieu of roll call: Charles Miller, Kentucky Cattlemen's Association; Billy Hurd, Monticello Banking Company; Dr. Harold Benson, Kentucky State University; Annette Walters, Former Farm Credit Services, Maysville, KY; Jane Jones, Financial Services Officer, Farm Credit Service; Sandy Ross, South Central Bank Ag Lender; Doug Lawson, Paducah Bank and Trust Ag Lender - Mr. Lawson also serves on the Kentucky Agriculture Resource Development Authority Board; Wayne Hunt, Christian County Grain Farmer - Mr. Hunt also serves on the Agricultural Development Board; Billy Ray Smith, Commissioner of Agriculture - Mr. Smith also serves on the Agricultural Development Board; Billy Joe Miles, Owensboro Farmer; Gordon Duke, Secretary of the Finance Cabinet - Mr. Duke is the former Chief Operating Officer of the Governor's Office of Agricultural Policy.

David Bratcher told us that under the statute the Board has the responsibility of electing a Chairman and Vice-Chairman and asked for nominations. Gordon Duke moved to nominate Billy Ray Smith as the Chairman; Doug Lawson seconded. Charles Miller

moved that the nomination come to a close. Without objection Commissioner Smith was elected. Commissioner Smith asked for nominations for Vice-Chair. Wayne Hunt made a motion to nominate Annette Walters as Vice-Chair. Commissioner Smith asked if there are any other nominations. Commissioner Smith asked for a motion to cease the nominations. Billy Joe Miles made the motion; Doug Lawson seconded. Commissioner Smith asked for discussion. The motion passed unanimously, Annette Walters appointed Vice-Chair.

David Bratcher reminded Board Members to pick up a travel voucher for reimbursement of cost associated with this meeting. He also asked members to review the Board Member list for needed corrections.

Commissioner Smith familiarized the group with the Government staff members present.

Enabling Legislation:

Mr. Bratcher noted that Board members had received a copy of the Long-Range Plan adopted by the Agricultural Development Board last year. The Agricultural Development Board oversees the Agricultural Development Fund. Wayne Hunt is on that Board as is Commissioner Smith who serves as Vice-Chair.

During the summer of 2001, the Agricultural Development Board solicited public comments for the Long-Range Plan. Strong sentiment was expressed for assistance in marketing as well as for a need for capital. Based on these comments the Agricultural Development Board developed a policy called Access To Capital. One of the points in this plan was to reactivate the KAFC Board.

Mr. Bratcher provided some background regarding KRS 247.940 – 247.978, KAFC's enabling legislation. The legislation for this organization was adopted by the General Assembly in 1984. This organization, for a period of time, served as an issuer of Aggie Bonds for first time farmers established under the Internal Revenue Code. Gene Royalty told us 18 real estate loans were made using Aggie Bonds, with the last one made in 1991. In every instance the lending bank bought the bonds. 10 have been repaid and there are still 8 loans outstanding.

He believes the reason this was not successful, was a bond was sold for each individual real estate transaction. With bond council, fees and so forth, it just wasn't competitive. Mr. Bratcher told us there was a secondary problem with the issuance of bonds. When this law was passed in 1984 there was a lot of activity in the Private Activity Industrial Revenue Bonds (which includes Aggie Bonds). There were a lot of situations where banks were buying the bonds, particularly for local projects. The Tax Equity Fiscal Responsibility Act of 1986 changed the federal law significantly as it related to industrial revenue bonds. In lay person's terms, this meant that banks could not take depositors' funds on which they were expensing interest and use those funds to buy bonds, the interest on which would be exempt from federal income tax. They could however, use

the banks equity to purchase bonds, but the appetite among the banking community dried up for industrial revenue bonds.

There are other states still with successful Aggie-Bond programs. We feel that is a viable alternative that we want to look at.

KAFC also established a revolving loan fund, with an initial allocation of \$500,000. The KAFC Board was required by regulation to meet and approve each individual loan. Staff believes the \$500,000 is still in place.

The legislation that we have is very broad. It does bestow upon this corporation the power to issue Aggie-Bonds. There is also language in that statute that says we have the authority to issue Industrial Revenue Bonds under KRS 103. KAFC also has the authority, as a corporation, to serve as a guarantor, to purchase loans from banks, to make direct loans and to own real estate.

Board members also had received a copy of House Bill 541, which was introduced by Roger Thomas and Tom McKee February 18, 2003. Commissioner Smith told us HB 541 could be considered in committee as early as February 20. This bill makes minor changes in the enabling legislation as well as changes to KRS 41, the statute that deals with the Link Deposit Program.

After discussion with Commissioner Smith and his staff, staff has proposed moving the Link Deposit Program to the Agriculture Finance Corporation. Gene Royalty explained the basics of the Link Deposit program.

The Link-Deposit Program began in the Treasurer's office several years ago. The funds come from the abandoned properties overseen by the Treasurer. Funds are invested in local banks at a lower rate of interest with the bank passing on the savings to the borrower. Currently banks receive these funds at 2% and loan to farmers at 5%. It is a program for the good agricultural borrower. There are about 16 banks that have participated and they have made loans in about 26 counties. While last fiscal year was the best year for the program, with 102 Link-Deposit loans made for a total of about \$6.8 million, It has been a program that has been difficult to market to the banks. The program has some guidelines adopted by the State Investment Commission, some of which are difficult for some banks to meet. The criteria includes:

- A loan to deposit ratio of greater than 70%
- A non-performing loan to capital ratio of less than 25%

Staff believes there may be approximately \$3 million available through the abandoned property program for Link Deposit. Mr. Royalty suggested that we put a link-deposit program in Agriculture Finance. Board members agreed that programs undertaken by KAFC should be done in concert with local lenders so as not to duplicate effort.

Considerable discussion occurred regarding the role KAFC could play in assisting value-added processors, thus enhancing the marketing needs addressed in the KADB Long Term Plan. Mr. Royalty noted that the Economic Development Cabinet has outstanding programs, but they focus heavily on job generation numbers. He offered an example of a processor who only employs 32 people. He told us that under normal conditions the cabinet would only look at \$10,000 a job. This processor is buying about \$15 million dollars worth of wheat from Kentucky producers. They have expressed an interest in expanding, especially in the storage area. Hopefully KAFC could develop a program that would assist a processor coming to Kentucky who would agree to contract with Kentucky producers to provide the raw product to be processed.

Mr. Bratcher explained that the reinvented Agriculture Finance Corporation would be somewhat like an umbrella agency. It could become a central point of contact for farmers who are looking for assistance and could house three different programs:

- Link-deposit Program
- Issuer of bonds for first time farmers
- Direct Loans

HB 541 makes changes to definitions to allow for greater flexibility in the loan programs of KAFC. During the discussion Board members noted that there was a need for assistance with first-time farmers, but that ample credit probably existed for farm production loans. Mr. Bratcher added that a young farmer might be eligible for some guaranteed loans through FSA or RDA. We cannot, as a corporation, be a guaranteed party of those guaranteed loan programs. The banks and Farm Credit can. We can buy in on the banks loan where we protect our portfolio with the guarantee shared proportionately with the bank, the collateral and in the risk. We can pass on to the borrower a fixed interest rate for the term of the loan. Mr. Hunt commented that the first time farmer may be a good place to see if we can get the counties to participate. Doug Lawson commented that hopefully the focus of this group is to open up opportunities for banks to become partners with this group.

Mr. Bratcher told us that, internally staff has talked about an application to the Agricultural Development Board, initially for about \$20 million to capitalize the corporation. The Agricultural Development Board will review this as an application, as they do any other application. A goal of the program should be to maximize use of the KAFC funds especially working with some of the companies that are trying to do some value added processing.

The Agricultural Development Board is very strong about making sure we help the farmer move up into the ownership structure. Gordon Duke asked the Agricultural Development Board whether KAFC should develop specific program and program recommendations prior to going to the Agricultural Development Board for application or just going for the funds to start with, then develop the program after we get the funds.

Commissioner Smith indicated a preference for the development of programs prior to submitting an application, including looking at what can be done with the statute as it currently exists. Gordon Duke noted that although the statute allows for a great deal of latitude the challenge is to decide where we start and where we place our priorities so as to have a dramatic impact in both the short and long term. He stressed the importance of developing some programs to help with agricultural processors or agriculture value added, anything that is going to support production in agriculture in this state to give them outlets, markets or vehicles for developing a product. He also expressed the importance of developing guidelines on what type of activity is eligible. He talked about the capital access program for small business, which sets up a loan loss reserve fund and told us this program could be adapted for agricultural lending.

Additional discussion focused on the need for educational and mentoring programs, perhaps not in a formal educational institution setting, but more at the farm level. It was generally agreed that most federal loan programs don't have an educational requirement. Charles Miller told us that we need to come up with a program that will make the banks want to make agricultural loans, especially to younger farmers who are better educated and who have a broader view of how agriculture ties into overall economic picture. There was some group discussion about federal guarantee programs.

Billy Joe Miles commented that if this program is just going to lend money and protect the banks we are not really going to do much for the state. He told us he feels that the tobacco settlement money has created a lot of prosperity. He feels that we should focus on young farmers and we need to leverage this money. An example of leverage would be to acquire an equity position in an existing company and move it to Kentucky so as to create the market for farmer owners. Ownership structure should be flexible to address the particular business plan of the organization. There was group discussion with several optional opportunities discussed.

There was further group discussion on varied points. Mr. Bratcher summarized the meeting's discussion by saying that the overriding things he has heard today is:

Explore whether there are capital programs for first time farmers who have had difficulty getting access.

Exploring the use of these dollars as a joint venture to allow farmers to expand their market opportunities and their wealth getting a percentage of ownership in a deal.

Billy Hurd that we need to prioritize these points. Based on today's discussion he feels that our priority needs to be processing and marketing with a focus on getting a greater portion of that dollar back to the producer. Along with that we cannot afford to overlook helping existing farmers to take advantage of those opportunities when they do come. Also, we need to address those new and emerging people that enable them to take

advantage of the efforts that are afforded to agriculture in this state because of the emphasis on processing and marketing

David Bratcher suggested that Gene and himself come up with an action plan setting priorities and get it to the group for critiquing.

Next Meeting Date:

There was discussion on the meeting schedule for this group. The next meeting is scheduled for March 19, 2003.

Adjourn:

The meeting adjourned at 12:00